Testimony of

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Mr. Chairman and members of the Subcommittee, thank you for the opportunity to appear today to discuss the implementation of the peanut program provisions of the Farm Security and Rural Investment Act of 2002 (2002 Act).

Let me begin by complimenting you and members of the full Committee for your foresight and leadership in working with the peanut industry to adopt a market-oriented program for peanuts that is similar to other basic commodities. This policy alters the course for the peanut industry, turning away from policies derived from New Deal era legislation and progressing to policies allowing producers to make decisions based on market conditions.

Summing up the initial two years of implementation of the new market-oriented peanut program, I believe the Department of Agriculture (USDA) has been very successful in overall implementation. In 2002, we faced the challenges of implementing the new program after the crop was planted, and we immediately instituted procedures to allow producers to use the non-recourse marketing loan program for 2002-crop peanuts. In 2003, we made great strides in gathering additional data needed to refine the program.

The non-recourse marketing loan programs that have operated for a number of years are quite different from the price support program to which the peanut industry was accustomed. Now, as is the case for other program crops, peanut producers can place their harvested production as collateral for Commodity Credit Corporation (CCC) marketing loans and repay the loans at the loan rate (plus interest) if prices are above the loan rate, or at less than the original loan rate when the market price is lower. This results in a benefit known as a marketing loan gain. As an alternative to placing peanuts under loan when market prices are below the loan rate, producers may elect to receive loan deficiency payments (LDP's) which are payments equal to the difference between the loan rate and the loan repayment rate. These features decrease the loan program's potential to result in CCC accumulation of stocks through forfeitures. Additionally, a producer's income is protected from the risk of downside market price fluctuations during the loan period.

Despite continuing import restrictions, for the first time in over 60 years, the markets are working and peanut prices are being determined in a more market-oriented environment. Based on current supply and demand market fundamentals we anticipate the industry will experience record food use of peanuts in the current 2003/2004 season, exports are being maintained at significant levels, peanut crush is showing strength and peanut imports have declined sharply. As you can see in the accompanying Chart 1, it is projected the 2003-2004 peanut crop stocks will reach relatively low levels this year. This takes into consideration total peanut use for the past several years and assumes similar trends will continue. Thus, today we believe there is cause for optimism in the new peanut market.

In addition to the non-recourse marketing loan, and similar to other program crops, the new peanut program provides for direct payments at a statutory rate and for counter-cyclical payments during periods of decreased market prices. These payments provide an additional safety net to producers with the flexibility to adjust their planting decisions to market conditions.

Under the new program, peanut producers may grow any quantity of peanuts and market them for food, export or crush. Under the prior program, producers had to have a poundage marketing quota in order to sell the peanuts in the more lucrative food market. Price support under the previous program was based upon a two-tiered support level that provided a high level of support for peanuts used in the domestic food market and a much lower level of support for peanuts that were to be exported or crushed for oil and meal.

In transitioning to the new marketing loan program, peanut producers are facing special challenges. Finding price information, not customarily a problem for other commodities with marketing loan provisions, is a unique problem with peanuts. For example, corn producers have a combination of mechanisms that provide price transparency in the marketplace. There are vast numbers of corn producers throughout the U.S. with multiple marketing options, including selling to feed yards, ethanol plants, and local elevators. Corn prices are openly reported on various market exchanges and by many market price reporting services. In stark contrast, there are a comparatively small number of peanut producers in the U.S. with limited sales options, no market exchange, and limited market price information sources. USDA has been working cooperatively with the industry and learning along with them the impacts of the new program. We believe these efforts will lead to solutions to the challenges that remain.

I would now like to provide you an overview of our implementation progress, examine the economic impacts of the program, and discuss the challenges that remain.

Program Implementation

As prescribed by the 2002 Act, USDA made payments to eligible quota holders under the so-called "buyout" program. Eligible quota holders could choose between accepting payments in one lump sum or in five equal installments at $0.11 per pound for 5 years, totaling $0.55 per pound.

USDA has paid over 95 percent of the peanut quota buyout payments, or nearly $1.24 billion to eligible quota holders. Of the 69,984 quota holders that enrolled for the buyout program, only 8 percent decided to accept the buyout payment in 5-annual installments. For quota holders that elected the annual installment option, payments will be issued annually during the month of January.

Owners of peanut base acres also have begun receiving payments under the Direct and Counter-cyclical Program (DCP) with respect to about 1.5 million base acres. National payment yields average almost 3,000 pounds per acre. CCC has issued $268 million in payments under the 2002 DCP and $128 million for the 2003 crop year. Additional counter-cyclical payments for the 2003 crop have just been announced and 2004 crop direct payments are being issued to eligible recipients.

During the 2002 crop year, the National Agricultural Statistics Service (NASS) estimates 1.66 million tons of peanuts were produced. Producers put virtually all peanuts under loan or received LDP's for the peanuts. Only 2,870 tons of peanuts were forfeited to CCC. Of those, CCC has sold 2,150 tons, receiving an average price of $357.62 per ton. As a matter of general policy, CCC does not accumulate stocks of forfeited commodities. Accordingly, commodities acquired by CCC through marketing loan forfeitures are sold into the marketplace as soon as possible.

Section 165 of The Federal Agriculture Improvement and Reform Act of 1996 authorizes the sale of CCC-owned commodities. The Farm Service Agency is responsible for CCC-owned commodity sales. CCC utilizes the following sales methods, to be consistent with other marketing loan commodities:

- make the peanuts available for immediate sale to the storing warehouse operator for a period up to 10 calendar days
- post sales availability to all interested parties on the Internet.

Unlike most other major commodities, CCC, under the provisions of the 2002 Act, is required to pay storage, handling and associated costs for peanuts pledged as loan collateral. Also, unlike other major commodities, peanut producers maintain very little, if any, on-farm storage. Since the cost of storage is borne by CCC, most peanuts are placed under the marketing loan program where they remain until marketed.

Loan Repayment Rate

The abolition of the old peanut program included the elimination of the two-tier quota/nonquota price support system that provided a lower level of government support for peanuts produced and marketed above quota levels established for a farm. Price discovery and transparency were of little significance in the previous program. Today, under the new peanut marketing loan program, price discovery and market transparency are vital because they represent the mechanisms by which the market communicates to producers how much their peanuts are worth.

The 2002 Act requires CCC to determine a repayment rate for peanuts under the marketing loan program that satisfies objectives that are identical to those for all other loan eligible commodities. The statutory loan repayment language outlines four objectives:

i) minimize potential loan forfeitures;

ii) minimize government stock accumulation;

iii) minimize Federal Government storage costs; and

iv) allow peanuts produced in the United States to be marketed freely and competitively, both domestically and internationally.

Although the other marketing loan programs have the same objectives, the way USDA derives the repayment rate for grain crops is different from that used for peanuts. For instance, corn loan repayment rates, typically known as posted county prices (or PCP's), are derived from major terminal market prices FSA obtains from major inland terminals and export ports. The terminal market prices are collected daily and reflect actual trades. In turn, the terminal prices are adjusted back to each county using publicly available differentials. The terminal prices,

differentials, and resulting PCP's are available daily at USDA Service Centers and on FSA's website for each county and for corn, as well as each of the other feed grain program crops, five classes of wheat, and nine oilseeds.

For peanuts, however, CCC announces a weekly loan repayment rate or national posted price. The loan repayment rate is calculated using available, but limited, domestic and international sales prices for peanuts. An average is computed using the prices collected each week. Because of the limited price discovery mechanism for peanuts, it is difficult for CCC to establish the weekly repayment rate.

In July of last year, at the end of the 2002 crop year, USDA convened an Interagency Peanut Task Force to fine-tune our price discovery process, focusing on both domestic and international prices. We assembled staff resources from 9 agencies in USDA.

The Peanut Task Force determined that the most critical component for a successful marketing loan program is accurate and timely price information, and that component remains elusive. Further, it was determined that price discovery in the peanut sector has been complicated by a lack of transparent, consistent, market-oriented data on transactions. Contributing to the lack of transparency is the small and highly competitive structure of peanut buyers. Also, unique marketing patterns include: 1) a lack of on-farm storage capacity; 2) provisions mandating government payment for storage and handling; and 3) a market in which participants were accustomed to numerous years of a quota price support system.

On October 22, 2003, USDA convened a meeting with representatives of all segments of the peanut industry, including growers, shellers, manufacturers and brokers. The purpose was to

discuss challenges related to price discovery and transparency and request their cooperation in developing solutions.

In subsequent meetings with the shelling segment, USDA requested more timely price reporting to enhance price discovery. Dating back to at least 1955, U.S. peanut shellers have provided the National Agricultural Statistics Service (NASS) with monthly price data to generate a published "all peanut price." USDA sought to improve on that price series and receive weekly verifiable price data, as well as prices by type of peanut and on a regional basis. However, the shelling segment indicated that rather than provide input to allow NASS to collect verifiable weekly price data, USDA should rely more heavily on shelled prices and prices from international sources. Currently, USDA has no statutory authority to implement mandatory peanut price reporting to assure we are receiving accurate and timely peanut price information.

Impacts of the 2002 Act

Perhaps the most significant impact of the new peanut legislation is that USDA no longer sets the minimum value of peanuts through the price support program. Market conditions now determine the price for peanuts. Despite the inherent problems and rough spots in this transition, the results are clear - - the industry is expecting record food use of peanuts this year, exports are being maintained at significant levels, imports have declined sharply, and peanut crush is showing strength.

Recent statistics show changes in planted acres have occurred since the enactment of the 2002 Act. Planted acreage in Virginia declined about 41 percent in 2003 compared to 2002.

Conversely, planted acreage in Florida increased 30 percent. In Oklahoma and Texas, planted acres declined 38 percent and 13 percent, respectively, from 2002. During the same period, producers in the states of Alabama, Georgia, North Carolina and South Carolina increased yields to the highest level since 2000. We believe these shifts reflect changes in production practices, such as increased irrigation, impacts of the quota buyout and the exit of producers who shifted from peanuts to other crops (Tables 1 and 2).

2003 Crop

During 2003, U.S. peanut farmers produced a high-yielding, high quality crop and, given current conditions in both domestic and international markets, should be in a good position to meet domestic and world market demands. The latest crop production report released by NASS reported just over 2 million tons of peanuts produced in the U.S. in 2003.

Of the total 2003 crop production, 16,809 loans have been disbursed with respect to over 1.66 million tons of peanuts, about four-fifths of total production. To date, about 672,000 tons of loan collateral have been redeemed.

According to the most recent USDA forecast, total U.S. food consumption of peanuts, the largest component of domestic use, is expected to be over 5 percent from last year.

Peanut Export Markets

In the two countries that are leading export competitors, Argentina and China, weather-related challenges have impacted world markets. Argentina experienced the effect of drought in major

peanut producing areas. While rainfall alleviated some drought conditions, the crop was planted late and it is estimated at 142,000 hectares, 10 percent below last year's plantings.

Industry reports indicate China's 2003 crop experienced a 1.5 million metric ton shortfall in peanut production due to extreme wet weather during harvest in major producing regions. Currently, it remains questionable whether China will resume exporting peanuts into the world market at previous-year's level.

USDA projects U.S. exports of the 2003 crop will reach 250,000 tons (in-shell). This is up slightly from the 2002 crop year. Given current international market conditions, some in the industry suggest exports could exceed 300,000 tons.

As depicted in Chart 2, U.S. peanut exports have been trending lower, declining from 385,805 tons in 1992 to 248,018 tons in 2003. Spikes in exports generally coincide with larger crops. The exception occurred in 1998 and 1999 where two moderately large crops combined to boost exports in 2000.

Since the decline in peanut exports has been ongoing, it is unlikely the continued decline in exports is due solely to provisions of the 2002 Act. In the years preceding 2002, the decline in peanut exports can be attributed to increased competition in international markets. During this period, both Argentina and China increased their export activities. Improvements in quality coupled with competitive pricing helped erode U.S. exports. Competitive pressures have intensified in recent years, particularly with the emergence of China as a major player in the market. China has doubled its exports since the mid-1990's and improved quality. Total

Chinese exports are now at 1.1 million metric tons annually. While a large portion of this increase has been to markets that previously did not import large quantities of peanuts, China has still managed to increase market share in nearly every market, including the European Union and Mexico. In both Europe and Mexico, this increased share of sales by China has come at the expense of peanuts from Argentina and the U.S. Argentina has been particularly hard hit due to their lower quality relative to the U.S. and has been one factor in the decline in Argentine peanut production in recent years. Other factors include poor harvests and export taxes that have reduced Argentina's competitiveness.

It should be noted that under the previous peanut program, producers could not carry over quota undermarketings and may have over-planted to ensure adequate production to meet quota, even if yields were poor. If production above quota resulted, excess peanuts were then exported, inflating prior years' shipments.

Remaining Challenges

I would like to now raise a few remaining challenges we face. USDA's Interagency Peanut Task Force continues to actively research, deliberate and work with the peanut industry on these and other issues that will enhance program delivery.

Price Discovery / Transparency

USDA will continue to commit resources to work with the peanut industry to improve price discovery mechanisms and provide more price transparency to both domestic and international markets. Further, USDA is considering a third party examination of the current peanut market

price discovery methods, options for improving price discovery for peanuts, and program implementation enhancements.

Shorten Loan Period

Under the new program farmers can have peanuts in storage during months that fall into the next crop year. Due to perishability factors, USDA became concerned about deterioration of CCC loan inventories, ability to re-sell and potential market impacts on peanuts during the current harvest period. Shortening the loan period would encourage producers to clear the market of peanuts before the next crop is harvested. USDA consulted with industry segments including producers, shellers and manufacturers to discuss the possibility of having marketing assistance loan on peanuts maturing no later than June 30 following the date in which the loan was made. To date, no consensus on this issue has been reached, but we will continue to conduct research to determine the feasibility of suggesting a change in the length of the loan period.

Loan Rates by Type

The 2002 Act provides for an average loan rate for the four types of peanuts grown in the U.S. (i.e. Runners, Spanish, Valencia, and Virginia). Values for each type vary based on end use. Using an average loan rate for the four types of peanuts could, over time, increase plantings of a type or types for which producers receive the greatest amount of program benefits and cause a shift in production by type and geographic region.

For example, county loan rates for the 2002 wheat crop were updated and, more importantly, differentiated by each of five classes of wheat: durum; hard red spring; hard red winter; soft red

winter; and soft white wheat. The updates and differentiation by class were done so that the county loan rates would better reflect recent market price relationships among counties and among classes, and to reduce the significant LDP-rate disparities that had existed in prior years when all-wheat loan rates had been used. USDA is evaluating the feasibility and potential benefits of implementing peanut loans by type using the wheat by class model.

Bio-competitive Agent to Minimize Aflatoxin Contamination

For the past several years, scientists have been researching and testing the commercial use of bio-competitive controls to minimize aflatoxin contamination. The bio-competitive agent is a different strain of a-flavus mold that competes, more aggressively, against the toxin-producing mold. The agent is applied as a field innoculate.

Recently, an application for full registration of the bio-competitive agent was submitted to the Environmental Protection Agency (EPA). If approved it may be difficult, if not impossible, for traditional visual testing for a-flavous mold in peanuts, as the "good mold" is indistinguishable from the "bad mold." Similar bio-competitive controls have been approved for use on cotton in Arizona.

The 2002 Act established the new Peanut Standards Board to provide consultation to USDA on quality and handling standards for domestically produced and imported peanuts. A working group within the Interagency Peanut Task Force, including representatives from AMS, is researching and reviewing various program implementation and grading options should EPA grant approval for the use of the bio-competitive agent. Upon completion of this review, USDA will ask the Peanut Standards Board to review this issue.

Segregation III Discounts

AMS inspectors visually test for the presence of Aspergillus flavus (a-flavus) mold when peanuts are delivered to buying points. Under certain climatic conditions a-flavus mold can cause aflatoxin contamination. Commodities found to contain aflatoxin lose value in the market because they require additional costs to process for food use or they cannot be used for animal or human consumption and must be crushed for oil and meal, thus reaping a lower return. In turn, such peanuts are designated Segregation III (Seg III) peanuts. Upon determination that peanuts are Seg III peanuts, the Farm Service Agency applies a discount of 65 percent of the loan value, ($124 per ton) to the peanuts when pledged as collateral for CCC loan, consistent with discounts applied to other commodities. The purpose of the 65 percent loan discount is to protect the value of CCC loan collateral. At the time peanuts are delivered to the buying point producers are given an option to sell Seg III peanuts at the discounted value or clean and re-grade them to determine if they will grade a higher value.

A grower group has met with USDA officials to express their concern that under the present system producers are unfairly penalized. According to the grower group, the buyer has been given more flexibility in using peanuts labeled Seg III, by allowing them to clean these peanuts and market them for full value in the commercial market. Growers, on the other hand, are penalized through the 65 percent discount in the loan rate. Again, upon completion of this review, USDA will ask the Peanut Standards Board to review this issue.

Interest in Trading Peanuts on Commodity Exchange

While there is no transparent price discovery for peanuts, USDA has learned the New York Board of Trade is examining the potential of trading peanuts on the exchange. Additional time

will be required to further review the potential size of the market, the impacts of the 2002 Act on U.S. production, risk points encountered in the industry from farmer to manufacturer, and how that risk is managed. If peanuts were traded on this, or another, commodity exchange, there would be better price discovery, much like other basic commodities under a marketing loan program.

Electronic Trading (Warehouse Receipts)

Electronic warehouse receipts can lead to efficiencies in marketing and handling of peanuts. Electronic warehouse receipts for peanuts were made available on a pilot basis in the fall of 2003 through EWR, Inc. To date, one company has used electronic warehouse receipts out of various warehouse locations in Texas, Oklahoma, Virginia, and North Carolina. A total of 793 electronic receipts have been issued, of which most were pledged as collateral for a marketing assistance loan.

There are many benefits to using electronic warehouse receipts. It is expected that more companies will make use of electronic warehouse receipt services beginning with the 2004 crop of peanuts, for the following reasons:

- reduction in legal risk, due to audit trails and increased validations;
- buyers and sellers receive immediate acknowledgement when a bid or offer is submitted, saving them time and money;
- increases competition, resulting in improved price discovery, since buyers and sellers may base bids and offers on up-to-the-minute market price information;

- eliminates inefficiencies and streamlines processes, since there is no need for mailroom handling or keypunching data;
- reduction in errors, because edits and validations are built in to prevent incomplete and incorrect data from being transmitted; and
- added security, because electronic warehouse receipts cannot be lost in the mail, misplaced in-house, or destroyed.

Conclusion

The peanut industry continues the process of moving toward a more market-oriented industry. As pricing data becomes more readily available, more timely and more reliable, USDA will continue our efforts to improve program delivery. As new issues arise we are committed to working with Congress and the peanut industry to work out viable solutions. While change may not come easily or as expeditiously as one would like, let me assure you that USDA is doing everything possible to assist the industry in transitioning to the peanut marketing loan program to meet Congress' intent of assuring it is as market-oriented as all of our other programs and one that will facilitate exports.

This concludes my testimony. I will now address any questions by the Committee Members.

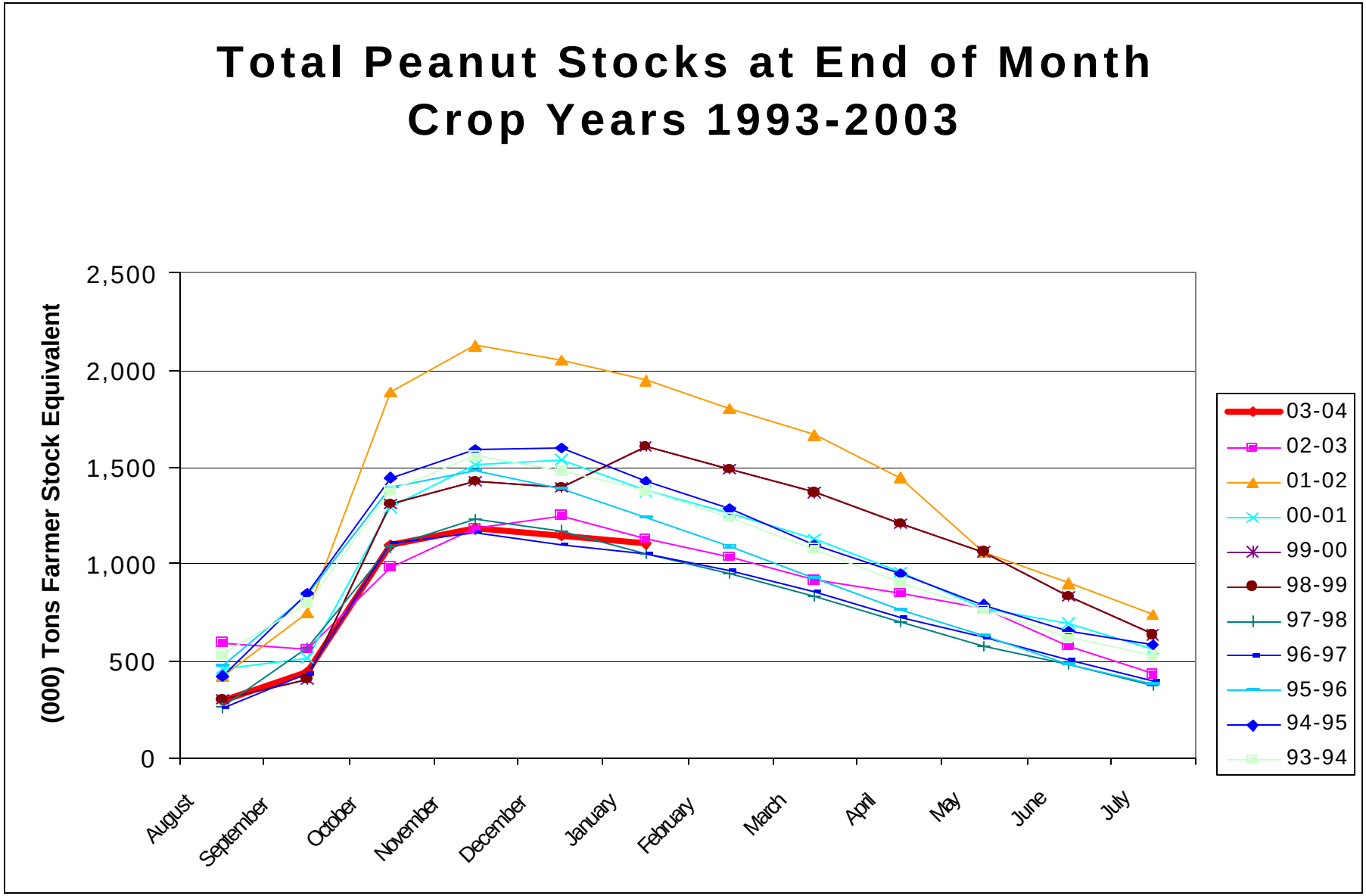
Table 1

NASS Peanut Planted Acres by State (1,000 Acres)			
State	**2002**	**2003**	**% Change 2002-2003**
AL	190	190	0
FL	96	125	30.21
GA	510	545	6.86
NM	18	18	0
NC	101	101	0
OK	60	37	(38.33)
SC	10	19	90.00
TX	315	275	(12.70)
VA	58	34	(41.38)
U.S.	1358	1344	(1.03)

Table 2

NASS Yields by State (Pounds per Acre)					
State	**2000**	**2001**	**2002**	**2003**	**% Change 2002-2003**
AL	1490	2675	2050	2750	34.15
FL	2485	3050	2300	3000	30.43
GA	2700	3330	2600	3450	32.69
NM	2115	3020	3000	2700	(10.00)
NC	2750	2910	2100	3200	52.38
OK	1800	2570	2800	2800	0
SC	2950	3000	2200	3400	54.55
TX	2540	2890	3100	3000	(3.23)
VA	2805	3130	2100	2900	38.10
U.S.	2404	3029	2561	3159	23.35

Chart 1


Total Peanut Stocks at End of Month
Crop Years 1993-2003
(000) Tons Farmer Stock Equivalent
2,500
2,000
1,500
1,000
500
0
August
September
October
November
December
January
February
March
April
May
June
July
03-04
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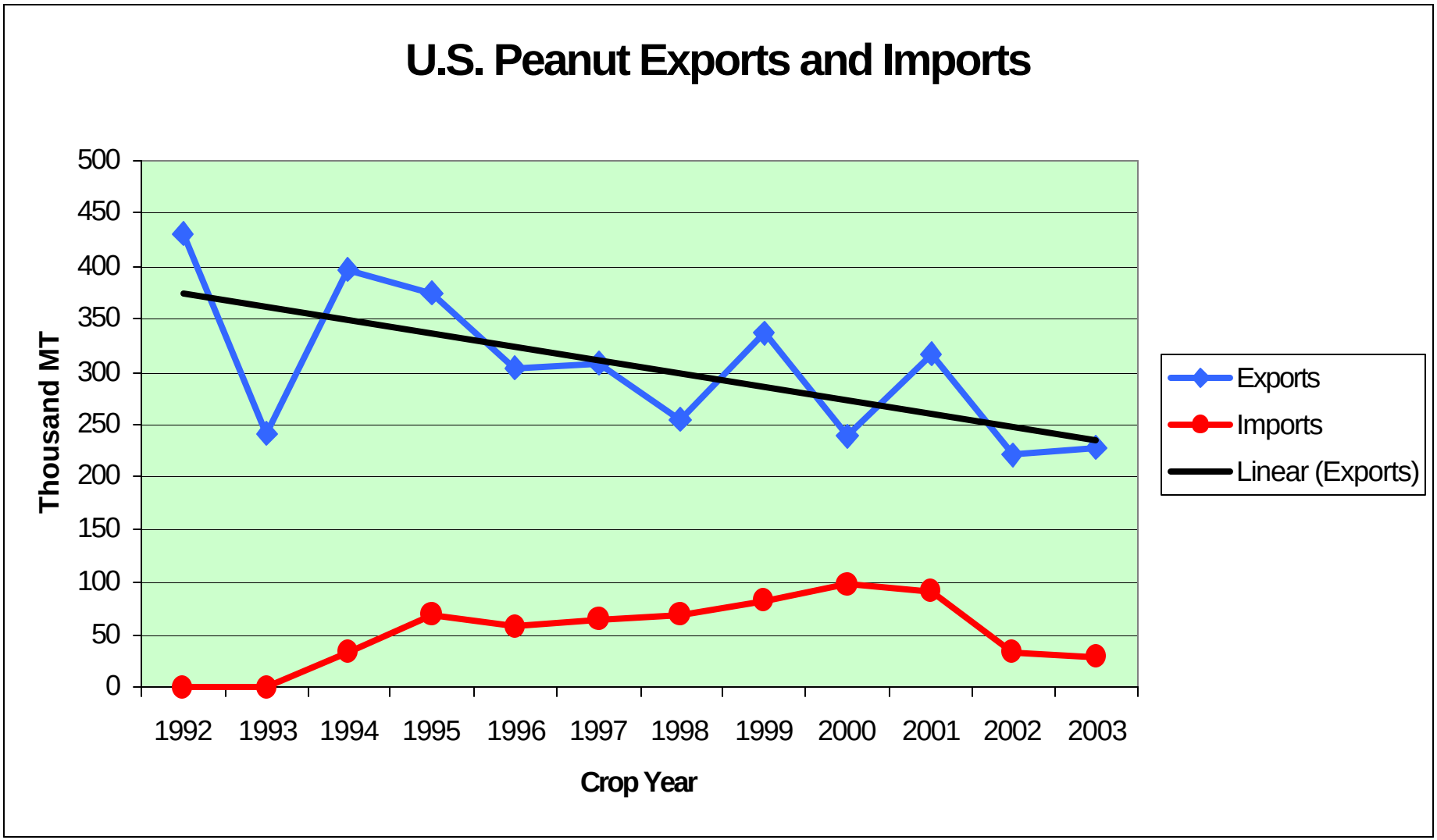
97-98
96-97
95-96
94-95
93-94

Chart 2



Note: 1992, 1994, 2001, and 2003 crops were all at 1.9 million tons (large crops). The 1998 crop was at 1.8 and 1999 was at 1.7 million tons. All other years ranged between 1.5 and 1.6 million tons.